Pushing the limits of outsourcing

Innovators reinvent the services relationship

For decades, cost savings was the dominant driver behind outsourcing. But sourcing motivations have changed. More than half of all CEOs now partner extensively with external providers to drive innovation. Among outperforming organizations, that percentage is even higher (59 percent). Similarly, two-thirds of growth-focused CIOs are partnering extensively to change the mix of skills, expertise and capabilities within their organizations.

In business today, most products and services are designed, developed and delivered by an integrated—often global—network of collaborators. As author and columnist Thomas Friedman put it, CEOs “rarely talk about ‘outsourcing’ these days. Their world is now so integrated that there is no ‘out’ and no ‘in’ anymore.”

Recently, we asked 97 C-suite executives about their aspirations for outsourcing relationships—both in terms of scope and what they aim to accomplish. Seven out of ten told us they plan to outsource for strategic reasons like driving growth and innovation. Based on their chief motivation, these organizations were categorized as:

- **Cost-cutters**—27 percent outsource their IT infrastructure to reduce operations costs
- **Growth-seekers**—37 percent outsource IT infrastructure, application management or business processes to achieve operational efficiencies and revenue growth
- **Innovators**—36 percent outsource multiple parts of the business to enable transformation and innovation

What we found most interesting was the progression of objectives across these three groups. When asked about a wide range of potential sourcing benefits, the only objective the majority of cost-cutters deemed very important was reducing operational costs and achieving balance sheet improvement. Simply put, cost-cutters want just one primary outcome from their outsourcing relationships: cost savings.
The majority of growth-seekers want to reduce costs too. But they also want faster time to market for new products and services, and increased efficiency and effectiveness across the entire value chain.

Innovators expect all of the above—and more. In addition to cost reduction, speed-to-market, and value chain efficiency, the majority of innovators want providers to help them:

- Drive front-office effectiveness (not just back-office)
- Better anticipate and respond to disruptive technological changes or market forces
- Proactively manage risk, compliance and security via technologies like predictive analytics
- Share risks and rewards based on business outcomes

Their outsourcing objectives are broad and ambitious. But they’re also indicative of a different type of relationship—one in which the service provider is far more integral to achieving desired business results. In fact, innovators are three times more likely to empower service providers with the flexibility to adapt technology infrastructure, applications and business processes as needed to deliver strategic business outcomes.

As innovators continue to expand the nature and scope of sourcing relationships, we expect other segments will shift their approaches as well. For instance, our findings suggest that cost-cutters are beginning to recognize the importance of broadening their sourcing focus beyond back-office operations into the front office, and enlisting partners’ help in transforming operations through better data integration and analytics. Tapping partners’ scale and leaning on them for a more proactive, holistic approach to managing security and risk are also next on their priority list.

Similarly, growth-seekers are interested in leveraging their providers’ global reach—as well as their expertise in proactively managing security, risk and compliance. Next up on innovators’ priority list is engaging partners who can help them deepen customer insights to improve customer experiences.

**Emergence of a new sourcing model**

With strategic partnering becoming increasingly prevalent, it’s important to consider the impact sourcing relationships can have—not only on business outcomes, but also on a company’s core business model and corporate culture. If innovation and transformation are critical components of your business strategy, how can prospective partners contribute?

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### Expanding expectations

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**Figure 1.** As a group, innovators have broader, more strategic objectives in mind for their sourcing relationships.
• Do they have proprietary insights or experiences that can provide headlights into future technological or market shifts?
• What competitive advantages could you gain from access to—or, even better, collaboration with—their R&D function?
• How can their expertise, assets, reach and network of partners help you develop new business models or expand into new markets?
• Do they have specialized capabilities that help deepen your understanding of customers and provide differentiated experiences?
• Will working with this provider over the next five years positively impact your organizational culture, making it more innovative and agile?
• How well do their strengths align with your particular business objectives?

This kind of criteria has significant implications for the entire ecosystem involved in the selection process—from sourcing decision makers to third-party advisors to service providers. Evaluation becomes much more difficult. For instance, how do you value greater agility, faster time-to-market or a more innovative culture—especially over the long term?

In addition to altering how service providers are selected, this new approach to sourcing also changes how firms work with them. Prioritizing both efficiency and innovation requires new governance models. Granular, task-oriented service agreements that dictate how—rather than what—tasks need to be performed hamper the ability of the organization and their providers to effect change, especially at the enterprise level. Compromises to accommodate the organization’s preferences can limit the partner’s ability to leverage standardization and scale. Companies will need to strike a balance that provides partners with both the ability and the incentive to attain desired business results. And to create room for achieving these broad, strategic objectives, the scope of the sourcing agreement may need to extend beyond individual processes or departments.

This new sourcing model could also cause companies to re-evaluate the number of service providers they choose to engage and the delivery model they use. When objectives are more strategic and touch more of the organization, services fragmentation can become quite costly and complex. Sourcing by process may seem optimal since it allows the firm to hire “best of breed” for a particular activity. But by perpetuating silos, it can actually sub-optimize the overall cost-to-value ratio, hinder agility and complicate the organizational change management necessary to achieve a wider range of business outcomes. As a result, companies may want to reduce the total number of providers to allow select strategic partners the opportunity to orchestrate greater transformation.

The choices companies make about providers—both how many and who to engage—also have implications in terms of social, political and economic risks. When organizations and providers are deeply intertwined, their performance, decisions and actions are linked, especially in the minds of customers and the general public. In an increasingly transparent world, businesses are judged by every facet of their global supply chains.

**Where’s your business headed?**

**Partner accordingly**

The sourcing of services is a decision with long-term significance. More than half of the companies we surveyed have been outsourcing for five years or longer.

Before entering this kind of long-term relationship, it’s worth considering the adage: You are who you associate with. Organizations need strategic providers that reflect the qualities and capabilities they aspire to have—the strengths that can lead to better business outcomes.
About the authors

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